Ministry for the Environment
Manatū Mō Te Taiao

Ministry for Primary Industries
Manatū Ahu Matua

To: Hon Damien O'Connor, Minister of Agriculture
Hon James Shaw, Minister of Climate Change

From: Charlotte Denny, Director – Natural Resources Policy, Ministry for Primary Industries
Sara Clarke, Director – Implementation, Ministry for the Environment

Lodgement of Cabinet Paper - Pricing system for agricultural emissions

Date	19 July 2023	**Reference**	MPI: B23-0529 MfE: BRF-3588

Decision required	**Date decision required by**
YES ☒ / NO ☐	25 July 2023

Purpose
This briefing seeks your agreement to lodge the appended paper and discussion document (by 3 August) for Cabinet's consideration on 7 August, seeking: • direction on progressing agricultural emissions pricing; and • approval to publicly consult on progressing an Order in Council (OiC) to defer New Zealand Emissions Trading Scheme (NZ ETS) obligations for farmers from 1 January 2024.

Contacts for telephone discussion (if required)			
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Context

1. On 5 April, DEV Committee considered and deferred decisions on a proposed alternative system to price agricultural emissions [DEV-23-MIN-0052 refers].

2. Together with the Prime Minister, you met with the Food and Fibre Leaders at Fieldays 2023. At this meeting the Prime Minister outlined a pathway forward for agricultural emissions pricing (option 1).

3. Subsequently, the Minister of Climate Change suggested an alternative way forward (option 2).

4. Decisions on which option to progress are required by Cabinet in early August 2023. This is to provide sufficient time to return to Cabinet pre-election for final policy decisions on the levy system *if* option one is progressed.

Pathway for agriculture emissions pricing policy and legislative decisions

5. The appended Cabinet paper provides two pathways to progress emissions pricing.

Option 1: Progressing policy decisions on agricultural emissions pricing before elections

6. This option seeks Cabinet decisions pre-election on an agricultural emissions farm-level levy (farm-level levy), including:
   a) establishing a standardised farm-level emissions calculation methodology by April 2024;
   b) in Quarter Four (Q4) of 2024, farmers and growers will face mandatory reporting of their emissions; and
   c) pricing farm-level emissions in Q4 2025.

7. The proposed farm-level levy builds on the section 215 report. The split-gas levy would be set at low levels initially and the revenue would be recycled back into the system for emissions reducing activities and operational costs. When setting levy prices, the primary consideration would be achieving emissions reductions in line with legislated targets and emissions budgets, taking into account additional factors.

8. Incentive payments would recognise the adoption of mitigation technologies, and an interim sequestration system would provide payments for some on-farm sequestration.

9. Primary legislation and supporting regulations are needed for the implementation of the pricing system before Q4 2024, including legislation outlining functions for Ministers.

10. If Cabinet prefers this option, we will prepare a detailed Cabinet paper on the farm-level levy to be considered by DEV on 23 August and Cabinet on 28 August. This is for approval to issue drafting instructions (see Next steps sections).

11. Timeframes for this option remain challenging. This option requires a truncated legislative and regulatory process which increases risks of drafting delays (which could occur due to having to clarify and develop policy detail), Treaty risks (if consultation is rushed), and implementation and delivery risks. Additional risks and implications of this option are outlined in the appended Cabinet paper.

Option 2: Deferring decisions on agricultural emissions pricing until after the election and starting with voluntary reporting now.

12. This option is a staged-decision making approach, where a standardised farm-level emissions calculation methodology is to be finalised by April 2024 and voluntary reporting enabled from Q4 2024. Subsequent decisions on mandatory reporting and pricing would be sought next year.

13. Implementation details (for example, implementation agencies and legislative approach) will be set out in the post-election Cabinet paper. Risks and implications of this option are outlined in the appended Cabinet paper.

Sequestration

14. Recognition of on-farm sequestration is a key component of pricing agricultural emissions work programme.

15. Regardless of which option Cabinet decides, work is progressing to enable the recognition of non-forest carbon removals, which includes on-farm sequestration:
    a) The Carbon Removals Strategy, agreed by Cabinet on 3 July, [CAB-23-MIN-0287 refers] and New Zealand Emissions Trading Scheme (NZ ETS) review will provide the further detail on the timing and approach to this; and
    b) Cabinet also agreed in-principle to include emissions and removals from non-forest land use types in New Zealand's NDC accounting subject to further work to understanding the implications of including these sources [CAB-23-SUB-0283 refers].

An Order in Council is needed in 2023 to defer farmers entering the NZ ETS from January 2024

16. The Cabinet paper also seeks approval to release a discussion document and consult, from mid-August for up to a three week period, on deferring reporting obligations under the NZ ETS for animals-farmers. These will begin on 1 January 2024, unless this date is deferred by Order in Council (OiC) (or the relevant Climate Change Response Act (CCRA) sections are repealed).

17. Consultation is a requirement of making an OiC under section 2B of the CCRA. Making the proposed OiC without the required consultation would be unlawful.

18. We propose delegating to the Prime Minister, Minister of Agriculture and Minister of Climate Change the authority to make final policy decisions on progressing this OiC following consultation and authorise the Minister of Climate Change to issue instructions for drafting the OiC in order to minimise timing risks.

19. Ministers could decide to expedite the OiC process so the OiC is made pre-election. However, this approach has significant timing risks and would require Cabinet agreement to prioritise this before the election.

Inter-agency consultation

20. The Treasury, Inland Revenue and the Department of the Prime Minister and Cabinet were consulted on this paper. Their feedback is outlined below.

Treasury

21. The Treasury have provided the following feedback on the Cabinet paper:
    a) are concerned with the levy system's ability to:
        i. meet targets, and
        ii. be fiscally sustainable while doing do; and
        iii. with low prices to limit impacts.

    The section 215 report notes that when setting levy prices, the primary consideration would be achieving emissions reductions in line with legislated targets and emissions budgets, taking into account additional factors; and
    b) further information is needed on the potential scale of deferring pricing decisions on emissions budgets and targets and the fiscal implications. More information on design changes to the pricing system (for example, levy prices, sequestration and incentive rates) is needed to better understand the implications of deferring decisions on a pricing system.

Regulatory Impact Statement and The Climate Implications of Policy Assessment (*CIPA)*

22. A regulatory impact analysis panel have assessed the proposal to progress agricultural emissions pricing and noted the paper does not meet Cabinet's requirement for a regulatory proposal as the paper seeks in-principles or interim policy decisions and has no regulatory impact analysis. This means this paper will be recorded as non-compliant and a 'supplementary analysis' will be required at the next point Cabinet decisions are made.

23. The panel also reviewed the Order in Council discussion document (**Appendix Two** of the Cabinet paper) and determined that it does not contain sufficient impact analysis to support Cabinet's decision to release it. This does not prevent Cabinet from deciding to release the discussion document. Our focus has been preparing a simple discussion document that sets out the issue relating to animals-farmer reporting obligations, and the proposal to defer these, as simply as possible.

24. The CIPA team has been consulted and confirms that the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

Inland Revenue

25. Inland revenue had no specific feedback.

Next steps

26. We propose the attached Cabinet paper, seeking agreement on a preferred option to progress agricultural greenhouse gas emissions pricing, be submitted directly to Cabinet for consideration on 7 August. Note that submitting papers direct to Cabinet requires the prior approval of the Prime Minister.

27. The following steps are needed to meet the 7 August Cabinet meeting:
    a) Ministers review - 20 July;
    b) Ministerial consultation- 28 July;
    c) lodge paper for Cabinet - 3 August; and
    d) Cabinet approval - 7 August.

28. If Cabinet agrees to option 1 (progress policy decisions for an agricultural greenhouse gas emissions levy including mandatory reporting and pricing pre-election), we will provide a second detailed Cabinet paper:
    a) second Cabinet paper to Ministers for review – 14 August;
    b) Ministerial clearance and consultation – 15 August;
    c) lodge papers for DEV - 17 August;
    d) DEV consideration – 23 August; and
    e) Cabinet approval - 28 August.

29. If Cabinet agrees to option 2, no further Cabinet decisions would be needed prior to the election as work to support standardised reporting is already underway.

Recommendations

30. **Agree** to provide feedback on the draft Cabinet paper to officials by Tuesday 25 July.

Yes / No

31. **Agree** to lodge the appended paper by 3 August, for Cabinet's consideration on 7 August.

Yes / No

32. **Note** the Prime Minister's prior approval will be required to submit the paper direct to Cabinet.

Noted

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Director Natural Resources Policy
Ministry for Primary Industries

Hon Damien O'Connor
Minister of Agriculture

/ 07 / 2023

Sara Clarke
Director Implementation
Ministry for the Environment

Hon James Shaw
Minister of Climate Change

/ 07 / 2023

Minister's comments

Appendix One: Cabinet paper *'Decisions to progress agricultural emissions pricing'*

In-confidence

Office of the Minister of Agriculture
Office of the Minister of Climate Change

Chair. Cabinet Decisions to progress agricultural greenhouse gas emissions pricing

Proposal

1. This paper seeks Cabinet's agreement on:
   1.1. a preferred option to progress an agricultural emissions pricing system; and
   1.2. to publicly consult on progressing an Order in Council to defer New Zealand Emissions Trading Scheme (NZ ETS) obligations for farmers from 1 January 2024.

Relation to government priorities

2. On 2 December 2020 the Government declared a climate emergency that, "demands a sufficiently ambitious, urgent, and coordinated response across government to meet the scale and complexity of the challenge" [CBC-20-MIN-0097 refers].

3. Reductions in agricultural emissions are required to slow the rate at which New Zealand contributes to climate change. The amount that agricultural emissions need to reduce by is expressed via:
   3.1. the all-sectors, all-gases emissions reduction target in New Zealand's Nationally Determined Contribution (NDC) set under the Paris Agreement;
   3.2. the domestic emission reduction targets laid out in the Climate Change Response Act 2002 (CCRA);
   3.3. the agricultural sub-budgets set under the domestic emissions budgets recently agreed by Cabinet [CAB-22-MIN-0152 refers]; and
   3.4. the all-sectors, all-gases emissions reduction target in New Zealand's Nationally Determined Contribution (NDC) set under the Paris Agreement.

4. Since 2008, emissions pricing has been the primary policy for reducing emissions in every sector of the economy, except agriculture. Pricing agricultural emissions is a key action in the Government's emissions reduction plan released in May 2022.

5. Achieving the purpose of the CCRA (as amended by the "Zero Carbon Act") is a key area of cooperation between the Labour and Green Parties.

Executive summary

6. This paper seeks Cabinet's decision on a preferred option to progress an agricultural greenhouse gas pricing system (pricing system):
   6.1. Option One seeks final policy decisions prior to the election to support mandatory reporting of farm-level emissions by quarter four (Q4) 2024 and pricing these emissions by Q4 2025. This option requires a truncated legislative and regulatory process with high implementation risks but incentivises emissions reduction from the agricultural sector sooner.
   6.2. Option Two proposes a staged decision-making process and seeks final decisions on an agricultural emissions pricing system after the election. A standardised farm-level emissions calculation methodology would be developed by April 2024, and voluntary emissions reporting enabled by Q4 2024. This option carries low implementation risk, but delays action towards placing a price on agricultural emissions, meaning more emissions reductions may be needed elsewhere to achieve our domestic and international emissions reduction targets.

7. The CCRA includes provisions for farmers to register and report in the NZ ETS from 1 January 2024 unless the date is deferred by an Order in Council[1] (OiC). We are seeking Cabinet's agreement to publicly consult on progressing an OiC to defer NZ ETS obligations for farmers from 1 January 2024 to 1 January 2026.

Background

8. Agriculture contributes 49 percent of Aotearoa New Zealand's greenhouse gas emissions. The agriculture sector therefore plays an important part in meeting our domestic (including our gross methane target) and international emissions reduction targets.

9. In 2019, Government agreed to work with the Food and Fibre Leaders on the He Waka Eke Noa – Primary Sector Climate Action Partnership (the Partnership) to design an alternative pricing system to agriculture entering the NZ ETS.

10. In 2022, Government received recommendations from the Partnership, advice from the Climate Change Commission (The Commission), and over 21,000 submissions during public consultation on a farm-level levy.

11. Following public consultation, we worked with the Food and Fibre Leaders to refine the pricing system. In December 2022, we released a report under section 215 of the CCRA that detailed a system to price agricultural emissions as an alternative to the NZ ETS.

[1] Under section 2A (5D) of the CCRA.

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12. The system was based on a farm-level split-gas levy designed to incentivise emission reductions in line with Aotearoa New Zealand's emissions reduction targets and maintain a viable and productive agriculture sector. It would include approximately 23,000 farmers and growers and covers approximately 96 percent of the agriculture sector's emissions.

13. On 5 April, the Cabinet Economic Development Committee considered a proposal to establish a farm-level agricultural emissions levy by 1 January 2025 [DEV-23-SUB-0052 refers]. The Committee agreed to defer decisions on the agricultural emissions levy.

14. We acknowledge there are unique circumstances for agriculture that mean pricing agricultural emissions by 1 January 2025 is no longer achievable and that we need more time to ensure the design of the pricing system is fit for purpose.

A decision is needed on preferred option to price agricultural emissions

15. Pricing agricultural emissions remains the top priority in incentivising emissions reductions from the agricultural sector in line with our domestic and international emissions reduction targets. While we remain committed to pricing agricultural emissions, we propose a phased approach is taken to achieving this. There are choices regarding the timing and approach of this phasing.

16. We are seeking Cabinet's agreement on a preferred option to progress an agricultural emissions pricing system. Following this direction, we would return to Cabinet seeking detailed decisions to enable drafting instructions for legislative changes, if required. **Appendix One** includes a table comparing these options.

Option One – Cabinet decisions pre-election on establishing mandatory emissions reporting by Q4 2024 and pricing by Q4 2025

17. At Fieldays 2023, the Prime Minister discussed with the Food and Fibre Leaders a proposed pathway for pricing agricultural emissions which includes:
    17.1. establishment of a standardised farm-level emissions calculation methodology;
    17.2. in Q4 of 2024, farmers and growers will face mandatory reporting of their farm's emissions; and
    17.3. in Q4 2025, farmers and growers will face a price on their farm's emissions through a farm-level levy system (levy system).

18. This option seeks Cabinet decisions on a levy system (outlined below) before the election so that legislation, supporting regulations and implementation activities can be delivered to support mandatory reporting by Q4 2024 and a levy system by Q4 2025.

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19. The levy system would build off the section 215 report and include:
    19.1. a split-gas levy that would price emissions from biogenic methane and long-lived gases (nitrous oxide and carbon dioxide) separately, set at low levels initially;
    19.2. when setting levy prices, the primary consideration would be achieving emissions reductions in line with legislated targets and emissions budgets, taking into account additional factors;
    19.3. revenue raised from the levy would be recycled back in the system, in line with a strategy that outlines spending priorities to reduce agricultural emissions and operate the system. The strategy would include operating costs, incentive and sequestration payments, and a dedicated fund for Māori landowners;
    19.3. to accelerate further emission reductions incentive payments will be provided for the uptake of approved mitigation practices and technologies;
    19.3. sequestration payments would recognise some on-farm vegetation in an interim sequestration system. On-farm sequestration would transition to the NZ ETS or other mechanisms in time;
    19.4. The Ministry for Primary Industries (MPI), Ministry for the Environment (MfE) and Inland Revenue (IR) would be responsible for implementing the system; and
    19.5. the costs associated with the establishment of the levy system and the first year of mandatory reporting will be paid for by the Crown. From Q4 2025 the levy would be fiscally sustainable and meet all ongoing administration and levy offset expenses (for example, sequestration and incentives payments).

20. This option has high implementation risks. To meet these timeframes, a truncated legislative and regulatory process is necessary, which increases the risk of issues that could impact implementation. Any delays could have significant impacts on implementation and delivery of a levy system.

21. If this option is preferred, a detailed Cabinet paper seeking final policy decisions on the reporting and levy system will be provided to Cabinet by the end of August, to allow the issuing of drafting instructions.

Option Two – Establishing standardised voluntary reporting now and defer decisions on agricultural emissions pricing until after the election

22. This option seeks Cabinet's agreement to a staged decision-making process. As in Option One, a standardised farm-level emissions calculation methodology will be developed and finalised by April 2024 at the latest. There are currently eleven different calculators for estimating on-farm emissions – a standardised calculation methodology would provide a consistent yardstick that could be used across the sector.

23. Voluntary reporting using this standardised calculation methodology would begin from Q4 2024. As this reporting would be voluntary, it would be developed outside of legislation.

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24. Decisions on mandatory reporting and agricultural emissions pricing system, including on timing, would be deferred until after the election. It is important the decision on mandatory reporting is taken at the same time as the decision on a pricing system to ensure workability and delivery. Developing a standardised voluntary reporting system outside of legislation in the short-term could support sector readiness, which is key to ensuring the implementation of the pricing system. Progressing standardised voluntary reporting via a phased approach will allow the system to be piloted and refined ahead of the introduction of mandatory reporting.

25. Deferring decisions until after election would mean mandatory reporting could not be implemented in 2024, and it is highly unlikely pricing could be in place by Q4 2025. This means, compared to Option One, there would likely be a longer period where no pricing mechanism is in place to incentivise emissions reductions from the agricultural sector. More emissions reductions may be needed elsewhere to achieve our domestic and international emissions reduction targets.

26. Following Cabinet decisions on a pricing system, subsequent legislation would set out the process for transitioning to a pricing system – including mandatory reporting.

27. Detailed regulations will also be required to support the pricing system, which may be developed in parallel to legislation.

28. If Option Two is the preferred option, no further Cabinet decisions would be needed prior to the election.

On-going work to recognise on-farm sequestration

29. A key component of pricing agricultural emissions is increasing recognition of carbon sequestration from on-farm vegetation.

30. Regardless of decisions on agricultural emissions pricing policy, work is progressing to increase recognition of non-forest carbon removals, which includes on farm sequestration. The Carbon Removals Strategy and NZ ETS review will provide the further detail on the timing and approach to this.

31. Cabinet agreed to progress the Carbon Removals Strategy on 3 July [CAB-23-MIN-0287 refers]. This includes the path to market entry, which aims to establish a clear pathway and data standards for inclusion of non-forest removals in the NZ ETS or other carbon markets.

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32. Cabinet agreed in-principle in the NDC Strategy paper to include emissions and removals from non-forest land use types in New Zealand's NDC accounting, subject to further work to understanding the implications of including these sources [CAB-23-SUB-0283 refers]. This will help alignment of emissions accounting between New Zealand's international targets and NZ ETS, if, or when the NZ ETS is expanded to include non-forest carbon removals.

Progressing an Order in Council to defer NZ ETS obligations for animals-farmers from 1 January 2024

33. Regardless of the preferred option to progress an agricultural emissions pricing system, monitoring, and reporting obligations for animals-farmers[2] (farmers) in the NZ ETS commence from 1 January 2024. Section 65 of the CCRA includes provisions for farmers to register and report in the NZ ETS from 1 January 2024 unless the date is deferred by an Order in Council[3] (OiC) (or the relevant sections are repealed).

34. There are significant risks in triggering these obligations, including:
    - 34.1. it is estimated to incorporate over 50,000 participants as the definition of an animals-farmer is not aligned to the thresholds and sub-sectors for participation that was proposed in the alternative agricultural emissions pricing system which would capture approximately 23,000 participants (such as, NZ ETS obligations also capture poultry, horses and pigs);
    - 34.2. there is not a system or regulations currently in place to support farmers to meet this requirement[4];
    - 34.3. the EPA has no existing capability to implement NZ ETS emission reporting for 50,000 farmers; and
    - 34.4. uncertainty for the agricultural sector as to their obligations and how their emissions will be priced.

Cabinet agreement is needed to consult and delegate functions to progress an OiC

35. Given the risks outlined above, we are seeking Cabinet's agreement to publicly consult on progressing an OiC[5] to defer NZ ETS obligations for farmers from 1 January 2024 to 1 January 2026. We propose consultation opens on 14 August 2023 and runs for a period of up to three weeks.

36. It is a statutory requirement to undertake consultation when making an OiC under s 2B of the CCRA[6]. Consultation needs to be progressed urgently before the election to ensure NZ ETS obligations do not start on 1 January 2024.

[2] CCRA definition of animal-farmer activities is "Farming, raising, growing, or keeping ruminant animals, pigs, horses or poultry for: Reward; or the purpose of trade in those animals, animal material or animal products taken or derived from those animals."
[3] Under section 2A (5D) of the CCRA.
[4] Otherwise, ETS reporting obligations would be triggered without the supporting regulation for participants to fulfil them.
[5] Under section 2A (5D) of the CCRA.
[6] Under section 2B (6) of the CCRA.

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37. Appendix Three outlines the timeframes and steps needed to progress the OiC before 1 January 2024.

38. The timeframes are tight for seeking Cabinet's approval of the OiC before 1 January 2024. To mitigate this risk, we seek Cabinet's agreement to delegate to the Prime Minister, Minister of Agriculture and Minister of Climate Change authority to make decisions in relation to deferral of the reporting requirements following consultation and issue drafting instructions.

39. We propose that legislation for an alternative system for pricing agricultural emissions would repeal any farmer-level NZ ETS obligations.

Treaty analysis

40. The Crown has obligations to Māori through instruments of statute, case law and settlement agreements. As a partner to the Treaty of Waitangi, the Government recognises the importance of the principles of partnership, participation and protection.

41. Iwi/Māori have significant interests in agribusiness and forestry, through both investment and settlement assets. It is important that Government engages meaningfully with Māori on any policy decisions regarding agricultural emissions policy that will impact Māori interests and assets.

42. Full analysis of the impacts on Māori will be provided when final policy decisions are sought.

Implementation

43. Primary legislation is required to enable the implementation of a reporting and pricing system, give power to the implementation agencies, and provide information sharing and data access between agencies.

44. Under both options, the MPI and MfE will continue working with the sector to determine and publish a standardised farm-level emissions calculation methodology, and implementation considerations across Government-funded and sector emission calculators. This will be completed by April 2024.

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Option One requires the Ministry for Primary Industries, Ministry for the Environment and Inland Revenue to implement the system

45. To support meeting timeframes for Option One (Q4 2024 mandatory reporting and Q4 2025 pricing), MPI, MfE, and IR must progress work required to implement the system. MPI are already progressing implementation by:
    45.1. engaging with the sector to further investigate and plan a farm-level emissions reporting framework, with a pathway towards pricing being subsequently introduced; and
    45.2. identifying what functionality would be necessary for enterprise Information and communication technology (ICT) within MPI, IR and, or The Environmental Protection Authority (EPA).

46. This work will inform Business Case(s) options to Cabinet to agree the preferred detailed approach to implementation and to draw down contingency funding.

Implementation decisions on Option Two will be decided later

47. MPI and MfE will be responsible for implementing voluntary emissions reporting. Implementation details for mandatory reporting and pricing would be decided later.

Cost-of-living Implications

48. In general, officials expect a low price on agricultural emissions will have no or minimal impacts on food prices. Further analysis will be provided when seeking final policy decisions on agricultural pricing.

49. Without reductions in agricultural emissions, New Zealand will need to reduce emissions elsewhere in the economy, generate more removals, or purchase more overseas emissions in order to achieve our first NDC. This may impact household costs for energy and fuel, depending on how the shortfall is met.

Financial Implications

50. Agencies were provided $15.4 million funding through Budget 2023. This funding will enable MPI and MfE (and IR if Option One, pricing agricultural emissions, is chosen) to continue to fund current implementation work. All establishment costs and the operating costs up until Q4 2025 will be met through the $149.8 million the tagged contingency funding envelope established at Budget 2023. A business case would be needed to access the tagged contingency to fund the full implementation costs, depending on the settings for the scheme. Details on the financial sustainability of the pricing policy will be provided at the point Cabinet takes final policy decisions.

Legislative Implications

51. Under Option One, to price agricultural emissions, an Agricultural Emissions Pricing Bill will need to be prioritised as a part of the 2024 Legislation Programme.

52. Under Option Two, voluntary reporting of emissions and defer pricing decisions, no change is required.

Risks

53. Risks relating to the two options to progress agricultural emissions pricing are found in **Appendix One.**

54. Risks related to triggering obligations for animals-farmers under the NZ ETS are outlined in paragraph 34.

Impact Analysis

55. Cabinet's impact analysis requirements apply to the proposals to progress agricultural emissions pricing. However, there is no accompanying Regulatory Impact Statement, and The Treasury has not exempted the proposals from the impact analysis requirements. Therefore, the paper does not meet Cabinet's requirements for regulatory proposals.

56. The Treasury's Regulatory Impact Analysis team, MfE, and MPI have agreed that supplementary analysis covering the full range of feasible options will be provided when Cabinet next makes decisions in relation to agriculture emissions pricing.

57. *Placeholder for OiC DD RIS statement]*

58. The Climate Implications of Policy Assessment (CIPA) team has been consulted and confirms that the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

Population Implications

59. Option One prices agricultural emissions sooner than Option Two, and so will be incentivised to reduce sooner. If agricultural emissions do not reduce, then further emissions reductions will be required elsewhere in the economy, more removals will be needed, or additional overseas emissions will be required, to reach our NDC1. Full analysis of population implications of pricing agricultural emissions will be provided when seeking final policy decisions.

60. If the OiC is not progressed to defer animals-farmer obligations from 1 January 2024, then potentially over 50,000 animals-farmers will be required to enter the NZ ETS. This would likely carry high administration and compliance costs for farmers.

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Human Rights

61. The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.[7]

Use of External Resources

62. No external resources were used to support this Cabinet paper. However, some contractors and, or specialist expertise supported the economic modelling (including an independent peer review), regulatory impact analysis, financial implications and implementation, and submissions analysis for the agricultural emissions pricing system.

63. Further detail on the use of external resource in policy development will be provided when seeking final policy decisions.

Consultation

64. MPI and MfE publicly consulted on a proposed split-gas farm-level levy to price agricultural emissions in October 2022. A summary of submissions from this consultation is proposed to be released, pending Cabinet decisions, following final policy decisions on an agricultural emissions pricing system are made.

65. The Treasury, Inland Revenue, and the Department of the Prime Minister and Cabinet (PAG) were consulted on this paper.

Proposed consultation process for the OiC

66. We propose consultation opens on 14 August and runs for a period of up to three weeks. Officials will take a traditional approach to consultation that will be comprised of a discussion document with targeted questions. It will also include:
    - 66.1. informing the He Waka Eke Noa Partnership prior to public consultation being announced;
    - 66.2. holding one webinar session for those that are not animals-farmers but who still may have an interest, for example with ENGOs; and
    - 66.3. engagement with iwi/Māori submitters who expressed an interest in agricultural emissions pricing.

Communications

67. [We will announce decisions via press release, email communications to agricultural emissions pricing stakeholders and publication on the implementation agencies' websites. A detailed communications plan will be developed jointly by our offices.]

68. Subject to Cabinet agreement, the discussion document for the OiC will be published on the Ministry for the Environment's website.

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[7] Noting that the Ministry of Justice is responsible for scrutinising proposed legislation and advising the Attorney-General on whether it meets Bill of Rights Act requirements.

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Proactive Release

69. [Following Cabinet consideration, we intend to consider the release of this paper and attachments on the Ministry for Environment website in whole or in part, subject to appropriate redactions.]

Recommendations

The Minister of Climate Change and Minister of Agriculture recommend that the Committee:

1. **Agree** to a preferred option for progressing decisions on an agricultural emissions levy system:

EITHER

Option 1:

2. **Agree** to seek final policy decisions, before elections, on the establishment and implementation of a farm-level, split-gas levy system (levy system) for agricultural emissions to enable mandatory reporting from quarter 4 (Q4) 2024 and pricing from Q4 2025.

3. **Invite** the Ministers to provide a detailed Cabinet paper by the end of August 2023 on a farm level system, described in the December 2022 Section 215 report, that includes the following features:
   a) price emissions from biogenic methane and long-lived gases (nitrous oxide and carbon dioxide) separately, set at low levels initially;
   b) levy prices set with the primary consideration being achieving emissions reductions in line with legislated targets and emissions budgets, taking into account additional factors such as availability and cost of on-farm mitigations and social, cultural and economic impacts on farmers, growers and communities;
   c) revenue raised from the levy would be recycled back in the system, in line with a strategy outlining spending priorities to mitigate agricultural emissions and operate the system;
   d) incentive payments would be available to recognise the uptake of mitigation technologies that reduce emissions;
   e) payments for some on-farm sequestration in an interim sequestration system. On-farm sequestration would transition to the NZ ETS in time;
   f) The Ministry for Primary Industries (MPI), Ministry for the Environment (MfE) and Inland Revenue (IR) will be responsible for implementing the system; and
   g) the costs associated with the establishment of the levy system and the first year of mandatory reporting will be paid for by the Crown from within the $149.8 million tagged operating contingency. From Q4 2025 the levy would be fiscally sustainable and meet all ongoing administration and levy offset expenses.

4. **Note** this approach will require policy decisions before the election and a Bill introduced in 2024 to legislate for mandatory reporting and pricing.

OR

Option Two:

5. **Agree** that voluntary reporting using a standardised calculation methodology will begin in Q4 2024.

6. **Note** Cabinet decisions on a mandatory reporting system and pricing agricultural emissions will be deferred until 2024.

Under either Option 1 or Option 2

7. **Note** that the intent is to include on-farm sequestration into the NZ ETS or other mechanisms, where practicable, and that the Carbon Removals Strategy and NZ ETS review will provide the further detail on the timing and approach to this.

8. **Note** that work is underway to develop a standardised farm-level emissions calculation methodology by April 2024 at the latest.

Progressing the Order in Council

9. **Note** that NZ ETS reporting obligations for animals-farmer activities will commence from 1 January 2024, unless deferred by an Order in Council.

10. **Agree** that the Minister of Climate Change will progress an Order in Council under section 2A(5D) of the CCRA in August 2023 to defer animal-farmers becoming NZ ETS participants from 1 January 2024, subject to consultation.

11. **Agree** to consult on progressing an Order in Council to defer obligations for animals-farmers under the NZ ETS under section 2A(5D) of the CCRA.

12. **Agree** that the appended discussion document be released for public consultation in August 2023.

13. **Authorise** the Minister of Climate Change to make decisions on any subsequent minor amendments to the discussion document not inconsistent with the Cabinet's approvals before its release.

14. **Delegate** to the Prime Minister, the Minister of Agriculture and the Minister of Climate Change authority to make final policy decisions on progressing this Order in Council and authorise the Minister of Climate Change to issue instructions for drafting the Order in Council following consultation.

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15. **Invite** the Minister of Climate Change to report back to Cabinet in December 2023 for Cabinet approval to submit the Order in Council to the Executive Council.

Authorised for lodgement

Hon Damien O'Connor
Minister of Agriculture

Hon James Shaw
Minister of Climate Change

CLASSIFICATION

Appendix One: Comparison of options

	Option One – Progressing pricing agricultural emissions pre-election	**Option Two – progress standardised voluntary reporting, defer pricing decisions**
Implementation risks	*High implementation risk* - A truncated legislative and regulatory process is necessary to enable mandatory reporting by Q4 2024. This truncated process increases the risk of issues which could impact implementation. Any delays could have significant impacts on implementation and delivery of a levy system.	*Low implementation risk* - More time provides opportunity to learn from standardised voluntary reporting system before making decisions on mandatory reporting/pricing. This timing will be influenced by how significantly the new pricing system differs to the one set out in the Section 215 report. Transitioning the voluntary system into a pricing system could potentially significantly increase implementation cost if IR is not involved. Deferring decisions until after election would mean mandatory reporting could not be implemented in 2024, and it is highly unlikely that pricing could be in place by Q4 2025.
Progress towards climate change targets	Agricultural emissions will be incentivised to reduce sooner. This option could also incentivise and reward "early adopters" sooner to take up mitigation technologies, the earlier those technologies will benefit from real-world experience and can be refined and scaled to market.	For this option, there is a longer period where no policy mechanism is in place to incentivise emissions reductions from the agricultural sector. Any significant delays to incentivising reductions in agricultural emissions could require New Zealand to reduce emissions elsewhere in the economy, generate more removals (e.g. from forestry), or purchase more overseas emissions to reach our NDC1. The cost of this will depend on how the shortfall in reductions is met and its relative economic costs, compared to the cost of agricultural emissions reductions.
Impacts on farmers and growers	Pricing agricultural emissions, even at very low prices, is likely to reduce revenue and output from the drystock and dairy sectors. To mitigate this, the proposed levy system is designed to set low levy prices for a set period initially.	Impacts on farmers and growers will depend on the final design of the pricing system. However, we expect that there will be low impact in a voluntary scheme.
Treaty risks	A truncated policy process could affect the Crown's ability to engage with Māori to understand the impacts of the policy	It is important that Government engages meaningfully with Māori on any policy decisions that may impact Māori, and this takes time. Progressing policy under tight timeframes or taking a new approach to pricing agricultural emissions without adequate engagement, carries Treaty risks.

Appendix Two: Order in Council Consultation Document

Appendix Three: Timeframe to progress Order in Council pre-election with consultation

August 2023	Cabinet approval to consult and delegate authority to the Prime Minister, Minister of Agriculture, and Minister of Climate Change to approve policy. Authorise the Minister of Climate Change to issue drafting instructions. Consultation (two to three weeks) *Assumptions to meet this timeframe: Cabinet compressed consultation period, no or minimal changes to consultation document.*
September 2023	Submissions analysis and policy development. Prime Minister, Minister of Agriculture and Minister of Climate Change decision in accordance with Cabinet's delegated authority. Issue drafting instructions. *Assumptions: one week for submissions analysis.*
October - November 2023	**Election 14 October** Draft OiC for Minister of Climate Change.
Early December 2023	Cabinet approval to submit the OiC for approval. OiC is approved and gazetted. 28-day period would need to be waived so the OiC can enter into force prior to 1 January. *Assumptions: in-coming Government prioritises OiC to be reviewed and approved at Cabinet in Early December.*
1 January 2024	Reporting obligations for animals-farmer commence unless deferred.
1 January 2025	Surrender obligations commence (at farm level for animals' activities unless deferred).

Deferral of NZ ETS reporting obligations for animals-farmer activities

Discussion document

Appendix refused under section 18(d) of the Act as the final version is already publicly available